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In The

Supreme Court of the United States

October Term, 1994

ARCO PRODUCTS CO.,

Petitioner,

vs.

GRAHAM OIL CO.,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

MOTION OF KAISER FOUNDATION HEALTH PLAN, INC. FOR LEAVE TO FILE BRIEF IN SUPPORT OF PETITION AND BRIEF *AMICUS CURIAE*

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MOTION OF *AMICUS CURIAE*, KAISER FOUNDATION HEALTH PLAN, INC. FOR LEAVE TO FILE BRIEF IN SUPPORT OF PETITION

A. Motion

Pursuant to Rule 37.2, Kaiser Foundation Health Plan, Inc. ("Kaiser") hereby moves for permission to file the following brief as amicus curiae in support of the pending petition for a writ of certiorari in the above-entitled appeal. Petitioner ARCO

Products Co. has consented to the filing of the proposed amicus brief. (*See* Appendix). Counsel for Respondent Graham Oil Co. informed Kaiser's counsel on July 12, 1995 that her client refused to consent. The reason given for the Respondent's refusal did not pertain to the merits of Kaiser's right to express its views concerning the pending petition.

B. Grounds For the Motion

As explained further in Part I of the proposed brief, Kaiser, a pioneer in organizing pre-paid health care services on a large scale, has a compelling interest in seeking reversal of the Court of Appeals' decision below. For over twenty years Kaiser has used arbitration as a vehicle for achieving just resolutions of disputes with its members without the frequent delays and additional expense of court litigation. Kaiser's arbitration program is assertedly threatened by the decision below because Kaiser's arbitration provision contains a general attorneys' fee/cost allocation clause that arguably conflicts with the provisions of particular federal statutes. Prompted by the decision below, Kaiser's adversaries are arguing that Kaiser's arbitration provision must be struck down *in toto*. Kaiser therefore believes that there is an urgent need for this Court to examine and reverse this ill-conceived Ninth Circuit precedent.

While Kaiser agrees with the excellent analysis set forth in Petitioner's brief, Kaiser's proposed amicus brief addresses other legal issues that are directly germane to the merits of the petition. In particular, Kaiser's brief explains that, assuming *arguendo* the correctness of the panel majority's interpretation of the Petroleum Marketing Practices Act ("PMPA"), the majority's interpretation of the disputed clauses of the ARCO/Graham Oil arbitration provision inexplicably ignores the most rudimentary principles of contract interpretation. In addition, Kaiser's brief demonstrates that the majority erred in choosing to decide the

legality of these clauses in the first place. Under this Court's recent decisions, *e.g., Vimar Seguros Y Reaseguros, S.A. v. M/V Sky Reefer*, __ U.S. __, 63 U.S.L.W. 4617, 1995 WL 360200 (June 19, 1995), the interpretation of the subject clauses and whether they are in a collision course with PMPA are matters that must be decided by the arbitrators in the first instance. Thus, an obvious solution to the problem at hand is an order summarily granting the petition and remanding to the Court of Appeals for reconsideration in light of *Vimar Seguros*.

On the basis of the foregoing, Kaiser respectfully asks that the Court allow its amicus brief to be filed so that the Court can consider the legal analysis set forth therein.

Respectfully submitted,

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Dated: July 17, 1995

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BRIEF *AMICUS CURIAE* OF KAISER FOUNDATION HEALTH PLAN, INC. IN SUPPORT OF PETITION

KAISER FOUNDATION HEALTH PLAN'S INTEREST AS *AMICUS CURIAE*

Kaiser Foundation Health Plan, Inc. ("Kaiser") submits this brief in support of petitioner ARCO Products' petition for a writ of certiorari. Kaiser does so because the decision below has been heard throughout the Ninth Circuit as the death knell for any

institutional arbitration provision that contains generally worded clauses that arguably alter the procedural rights or remedies that attach to court litigation of a federal statutory claim. The arbitration programs of Kaiser and other organizations, both within and outside the health care industry, are under attack because their arbitration agreements contain one or more generally worded clauses similar to those that were condemned by the majority panel opinion in this case.

Kaiser, a non-profit corporation, and its affiliates operate health maintenance organizations ("HMOs") in California and other parts of the United States. These HMOs arrange for health care services to millions of people under medical and hospital service agreements entered into with government agencies, private employers, union-management welfare funds, and individual subscribers. The basic terms of these service agreements are standard provisions that are subject to review and approval by state licensing agencies and the U.S. Department of Health and Human Services. Kaiser is regulated by the latter agency because Kaiser's HMOs are federally qualified under the federal Health Maintenance Organization Act of 1973, 42 U.S.C. § 300e *et seq.*

The service agreements of the Kaiser HMOs in California and in several other regions of the United States include standard arbitration provisions. Kaiser's California arbitration provision, which applies to more than 4 million members, encompasses any claim that

> arises from alleged violation of any duty incident to or arising out of this Agreement, including any claim for medical or hospital negligence or for premises liability, irrespective of the legal theories upon which the claim is asserted.

The enforceability of this provision is governed by the Federal Arbitration Act, 9 U.S.C. § 1 *et seq.*, because the performance of the underlying HMO agreements involve and affect interstate commerce.

The Kaiser arbitration provision provides, *inter alia*, that each side must bear its own attorneys' fees and costs, except for the expenses of the neutral arbitrator, which are borne equally. This generally worded "pay your own" attorneys' fee/cost clause reflects California's statutory "pay your own" rule that applies when a California arbitration agreement is silent regarding the recoverability of fees and costs. Calif. Code of Civ. Pro. § 1284.2; *Dickinson v. Kaiser Foundation Hospitals*, 112 Cal. App. 3d 952, 954, 169 Cal. Rptr. 493 (1980).

The Kaiser California HMOs have used arbitration for more than twenty years. In 1976, the California Supreme Court held that the provision is not an illegal "adhesion contract" because arbitration is favored by public policy and does not impair the parties' substantive rights and obligations. *Madden v. Kaiser Foundation Hospitals*, 17 Cal. 3d 699, 710-12, 131 Cal. Rptr. 882 (1976).

Kaiser's interests are adversely affected by the opinion below. While most Kaiser arbitrations involve state law claims of medical malpractice, many arbitrated cases include claims that are asserted under various federal and state statutes that provide for attorneys' fee awards to the prevailing party in court *actions* that are instituted under these statutes. In the wake of the Court of Appeals' opinion, claimants who assert these statutory claims are now arguing that the *entire* arbitration provision is unenforceable because it requires the parties to bear their own attorneys' fees and costs. Whether or not these statutory claims are joined with common law malpractice claims, the Court of Appeals' opinion is a dangerous precedent that is spawning considerable litigation

that seeks the wholesale nullification of institutional arbitration provisions that contain "pay your own" attorneys' fee/cost clauses. Kaiser therefore has a very strong interest in persuading this Court to rectify the Ninth Circuit's error.

SUMMARY OF ARGUMENT

Like the arbitration agreements used by Kaiser and other organizations, the ARCO/Graham Oil contract contains a pre-dispute arbitration provision that obligates the parties to arbitrate a wide variety of claims that relate to the parties' contractual relationship. The universe of arbitrable claims far exceeds those that are subject to the Petroleum Marketing Practices Act ("PMPA"). In this context, the disputed clauses of the ARCO/ Graham arbitration provision are lawful *on their face*. Furthermore, under well recognized principles of contract interpretation, the legality of the disputed clauses is easily preserved by construing them as applying only to disputes that are not subject to PMPA. Thus, the majority opinion below plainly erred in finding that the disputed clauses are illegal.

The meaning and validity of these clauses, however, are for the arbitrators to decide in the first instance. Whether the clauses contemplate a remedial scheme that conflicts with PMPA is a matter that the parties agreed to submit to arbitration. *If* the arbitrators render an award that offends PMPA, the lower courts can then be called upon to vacate the award in accordance with the standards set forth in section 10 of the Federal Arbitration Act, 9 U.S.C. § 10 and *First Options of Chicago, Inc. v. Kaplan*, __U.S. __, 115 S. Ct. 1920, 1923-24, 63 U.S.L.W. 4459 (May 22, 1995).

If the challenged clauses are illegal and the severability issue must be reached, the Ninth Circuit's decision to strike down the

entire arbitration provision defies rudimentary contract analysis and subverts the strong federal policy in favor of arbitration. The majority opinion can be read as creating a presumption of non-severability that will nullify any arbitration provision that contains a subsidiary term that is found to transgress a federal statute.

ARGUMENT

I. The Court of Appeals Erred in Concluding That the Allegedly Offensive Clauses Are Illegal.

For purposes of the present analysis, Kaiser will assume *arguendo* that the majority opinion below correctly concluded that the PMPA provisions concerning the recoverability of attorneys' fees and punitive damages and the applicable limitations period are both non-waivable and intended to apply to contractual arbitrations.[1] The majority, however, erred in assuming that this conclusion necessarily rendered the disputed contract clauses illegal *per se*. Under fundamental principles of contract interpretation, the contract terms in question must be construed as facially lawful but subordinate to the overriding requirements of PMPA.

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1. Whether a fee/cost shifting statute applies to arbitration proceedings is an issue that turns on the legislative intent behind the statute. While fee shifting may make sense in the context of expensive court litigation, it can interfere with the speed and economy of arbitration proceedings. Depending on the context, it may be appropriate to limit a statutory fee shifting provision to the fees incurred in prosecuting or defending civil court *actions*, particularly if the wording of the statute is so limited. *See, e.g., Graphic Communications Union v. GCIU-Employer Retirement Plan*, 917 F.2d 1184, 1188-89 (9th Cir. 1990) (upholding equal cost sharing clause in arbitration agreement against contention that it violated ERISA's fee/cost shifting provision); *Cann v. Carpenters' Pension Trust Fund*, 989 F.2d 313, 315-17 (9th Cir. 1993) (holding that ERISA's fee/cost shifting statute does not apply to fees incurred before commencement of court litigation).

The substantive scope of the ARCO arbitration provision is by no means limited to claims under PMPA. The provision applies to "any dispute or controversy relating to or arising out of the" ARCO/Graham distributorship agreement. The broad scope of the arbitration provision clearly embraces common law tort claims and a wide variety of non-PMPA statutory claims that do not implicate a statutory right to attorneys' fees, punitive damages, or a specified limitations period. One must therefore conclude that the attorneys' fee, punitive damages, and limitations terms of the provision are not illegal on their face because there are any number of dispute settings in which these terms would be beyond reproach. Because the meaning of a contract is determined as of the time when the contract was made, *e.g.*, 4 *Williston, Law of Contracts* § 601 at 306 (3rd W. Jaeger ed. 1961), it is implausible that the parties intended that the subject clauses would apply only to a subset of disputes within the broad substantive reach of their arbitration agreement.

Given the assumption made at the outset, the real issue is whether the clauses in question should be *construed* as illegal in the context of this case because they conflict with PMPA. The putative conflict, however, is readily avoided with the aid of conventional rules of contract interpretation.

In construing a contract, a court ordinarily proceeds from the presumption that the parties intended the contract's terms to have a lawful meaning. *E.g., Restatement of the Law, Second, Contracts* § 203(a); *Williston, supra*, § 620 at 747-51. Another axiom holds that relevant statutes "enter into and form a part of the contract as fully as if expressly incorporated therein." *Williston, supra* § 615 at 597. In the context of the present case, these principles point to a straightforward interpretation: the overriding PMPA provisions are deemed to be a part of the contract and qualify the express contract clauses in the context of a claim governed by PMPA. Any other conclusion would force

contract drafters to undertake the absurd task of expressly enumerating every type of claim that is possibly exempt from the generally worded clauses.

In sum, even if the public policy favoring arbitration is ignored, traditional contract analysis compels the conclusion that the disputed contract clauses are not illegal, either on their face or as they would likely be applied in this case. Thus there is no need to even reach the issue of whether these clauses are severable from the main arbitration covenant.

II. The Interpretation of the Disputed Clauses Should First Be Decided by the Arbitrators.

What has been said so far rests on the dubious assumption that *de novo* judicial interpretation of the challenged clauses is appropriate at the early stage of a motion to compel arbitration. This Court, however, has held that the courts should not speculate on whether arbitrators will construe a contract so as to place it in conflict with the remedial provisions of a federal statute. Most recently, in *Vimar Seguros Y Reaseguros, S.A. v. M/V Sky Reefer*, __ U.S. __, 63 U.S.L.W. 4617, 1995 WL 360200 (June 19, 1995), a party seeking to avoid arbitration argued that a foreign arbitration panel would construe the arbitration agreement as eliminating the protections afforded by the federal Carriage of Goods by Sea Act. The Court held that this challenge was premature because the arbitrators had not yet been afforded an opportunity to construe the contract. *Id.* at *8 [Westlaw pagination].

The Court's recent decision in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, __ U.S. __, 115 S. Ct. 1212, 63 U.S.L.W. 4195 (Mar. 6, 1995) tacitly confirms that the *Vimar Seguros* approach is fully applicable to the remedial issues herein. In *Mastrobuono*, individual investors were awarded punitive

damages in an arbitration over various claims they asserted against Shearson Lehman. The lower courts vacated the punitive damages award, holding that the arbitrators should have construed the choice of law clause of the arbitration agreement as incorporating a state law prohibition against arbitral awards of punitive damages. Although this Court upheld the arbitrators' interpretation based on the Court's own *de novo* examination of the contract, (*id.* at 1215 n. 1 & 1217 n. 4), neither Justice Stevens' majority opinion nor Justice Thomas' dissenting opinion suggests that the arbitrators lacked the power in the first instance to construe the extent of their remedial authority under the contract.[2]

In the case at hand, the Ninth Circuit clearly erred in deciding the legality of the disputed clauses before these issues were determined by the arbitrators in accordance with the parties' agreement. Under these circumstances, the Court may choose to issue an order summarily granting the petition herein and remanding to the Court of Appeals for reconsideration in light of *Vimar Seguros, supra.*

III. Assuming the Disputed Clauses Are Illegal, the Court of Appeals Erred in Refusing to Sever the Clauses from the Main Arbitration Covenant.

If the severability issue must be reached, it is difficult to fathom how and why the majority below arrived at their finding that the offensive clauses are not severable from the parties' basic agreement to submit the claims in question to arbitration. The

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2. Regarding whether the arbitrators' decision should be accorded deference, both Justice Stevens' and Justice Thomas' opinions (*id.* at 1215 n.1 & 1219 n.1) expressly left this issue open pending *First Options of Chicago, Inc. v. Kaplan*, __ U.S. __, 115 S. Ct. 1920, 1923-24, 63 U.S.L.W.4459 (May 22, 1995) (recognizing deferential standard applies to review of arbitrators' decisions on arbitrable issues).

contractual limitations period has had no impact on this case because plaintiffs commenced their action well within the specified time period. In any event, there is no functional interdependence between the arbitration process and the duration of the applicable statute of limitations.

The same holds true with respect to the challenged attorneys' fee and punitive damage clauses. As observed by Professor Corbin:

> When [a provision excluding a remedy] is so declared [to be in violation of public policy], it has almost always been held that the validity of the bargain in other respects is not impaired. The illegal provision is merely disregarded.

6A *Corbin On Contracts* §1527 at 779 (West 1962).

Any lingering doubt on the severability issue should be resolved by the public policy favoring arbitration that has been repeatedly reaffirmed by this Court. The importance of this policy is exemplified by the California Supreme Court's decision in *Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d 807, 623 P.2d 165, 171 Cal. Rptr. 604 (1981), in which the California court was faced with a far more difficult severability issue than the one presented here. There, the plaintiff appealed from an adverse award rendered under an arbitration provision that designated an arbitral panel that was clearly biased in favor of his adversary. Although the California court held that the arbitrator designation term was unconscionable, it was careful not to nullify the entire arbitration agreement. Rather, the court held that "[i]n light of the strong public policy of this state in favor of resolving disputes by arbitration[,]" the remainder of the arbitration provision was still valid. The court accordingly directed the trial court, on remand, to order arbitration before a different arbitrator chosen by the parties or appointed by the trial court. *Id.* at 831.

The challenged clauses herein are collateral appendages that can be cleanly excised without affecting either the parties' agreement to arbitrate or the arbitral forum chosen for this purpose. A judicial severing of the disputed clauses would only enhance Graham Oil's remedial rights. On these facts, the majority opinion below can only be seen as turning this Court's longstanding pro-arbitration policy on its head.

CONCLUSION

On the basis of the foregoing, Kaiser respectfully urges the Court to accept this case for full review or, in the alternative, to grant the petition for the purpose of a summary remand to the Court of Appeals for reconsideration in accordance with *Vimar Seguros, supra.*

Respectfully submitted,

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July 14, 1995

BY FAX (510) 451-1711
BY FEDERAL EXPRESS

Mr. Kennedy P. Richardson
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Re: ARCO Products Co. v. Graham Oil Co. — Amicus Brief

Dear Mr. Richardson:

This letter confirms that Atlantic Richfield Company, and its division ARCO Products Company, consents to the filing of an amicus curiae brief by Kaiser Foundation Health Plan in support of ARCO's petition for writ of certiorari in this case.

Very truly yours,
s/ Randolph C. Foster
Randolph C. Foster

RCF:bjc